

Message Text

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ACTION ARA-20

INFO OCT-01 ISO-00 AID-20 CIAE-00 COME-00 EB-11 FRB-02

INR-10 NSAE-00 RSC-01 TRSE-00 XMB-07 OPIC-12 SPC-03

CIEP-02 LAB-06 SIL-01 OMB-01 PA-04 PRS-01 USIA-15

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TO SECSTATE WASHDC 1987

INFO AMCONSUL RIO DE JANEIRO

AMCONSUL SAO PAULO

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E.O. 11652: N/A

TAGS: EFIN, BR

SUBJECT: REMOVAL OF 40 PERCENT DEPOSIT

1. FOLLOWING REPORT ON IMPACT OF REMOVAL 40 PERCENT DEPOSIT REQUIREMENT ON FOREIGN FINANCIAL LOANS TO BRAZIL WAS PREPARED BY CONGEN SAO PAULO.

2. CONGEN HAS SAMPLED 20 OF THE LARGER SAO PAULO BANKS TO DETERMINE REACTION OF THE LIFTING OF THE 40 PERCENT DEPOSIT REQUIREMENT. MOST BANKERS WERE SURPRISED THAT SUCH A MOVE WAS TAKEN BEFORE MARCH 15. IN RETROSPECT, THIS MOVE IS VIEWED: (A) AS A METHOD OF INJECTING LIQUIDITY INTO A BONEDRY CREDIT SITUATION, EASED ONLY SOMEWHAT BY THE INCREASE IN REDISCOUNTS ANNOUNCED SEVERAL DAYS EARLIER; AND (B) AS A MEANS OF TESTING THE WATER, TO DETERMINE HOW THE INTERNATIONAL FINANCIAL COMMUNITY VIEWS BRAZIL TODAY, UNDER INTERNATIONAL CIRCUMSTANCES WHICH ARE QUITE DIFFERENT FROM THE PERIOD PRIOR TO AUGUST 31 WHEN BRAZIL WAS LAST IN THE MARKET.

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3. ALL BANKS REPORT VERY HIGH LOCAL DEMAND FOR LOAN FUNDS. WHILE THE COST OF FOREIGN BORROWING HAS INCREASED, COMPARED TO LAST YEAR, IT REMAINS CHEAPER THAN LOCAL COST FINANCING AND BANKS HAVE WITNESSED A REAL SCRAMBLE FOR FOREIGN FUNDS FROM BRAZILIAN AND MULTINATIONAL CLIENTS.

4. ESTIMATES FOR LOAN REGISTRATIONS DURING FIRST 10 WORKING DAYS RANGE UP TO \$500 MILLION. SIZE OF INITIAL REGISTRATIONS ATTRIBUTABLE TO FIVE MONTH BACKLOG OF APPLICATIONS, WHICH HAD BEEN PREPARED EARLIER AND HELD BY BANKS IN ANTICIPATION OF SOME CHANGE IN DEPOSIT REQUIREMENT. THERE ALSO APPEARS TO BE A HEDGING FACTOR AT WORK; A NUMBER OF FIRMS REPORTEDLY ARE CONTRACTING FOR FUNDS BEYOND THEIR IMMEDIATE REQUIREMENTS IN ANTICIPATION THAT THE AUTHORITIES MAY IMPOSE NEW RESTRICTIONS AFTER A RELATIVELY BRIEF PERIOD.

5. JAPANESE BANKS, WHICH WERE A MAJOR FACTOR LAST YEAR, ARE NOW OUT OF THE MARKET. HEADS OF FUJI AND MITSUI BANKS IN SAO PAULO HAVE CONFIRMED TO CONGEN OFFICERS THAT JAPANESE MINISTRY OF FINANCE HAS PLACED A STRINGENT REVIEW PROCESS ON ALL LOANS ABOVE \$1 MILLIONS, WHICH EFFECTIVELY PRECLUDES JAPANESE PARTICIPATION IN NEW LOANS TO BRAZIL. GOJ HAS DETERMINED THAT EQUITY/LOAN PACKAGES FOR MAJOR PROJECTS AGREED TO OVER THE PAST YEAR IN STEEL, PETROCHEMICALS, AGRICULTURE AND OTHER SECTORS, WILL GO FORWARD BUT THAT NO NEW PROJECTS WILL BE FINANCED. EURODOLLAR SITUATION MUCH TIGHTER THAN LAST YEAR AND APPARENTLY, WITH REMOVAL OF US CAPITAL EXPORT CONTROLS, THERE IS A MARKED SHIFT TOWARD US-SOURCED FINANCING. FRENCH CONSORTIA (WITH THE ASSISTANCE OF TAX TREATY BENEFITS) ARE STILL ACTIVE AS ARE SWISS BANKS BUT BRITISH AND GERMAN BANKS GENERALLY MUCH LESS SO. NEVERTHELESS, EURODOLLAR MARKET CONTINUES TO BE THE PRIMARY SOURCE FOR NEW LOANS.

6. OPINION IS MIXED WHETHER BRAZIL IS STILL ATTRACTIVE ENOUGH UNDER CURRENT CONDITIONS TO BE ABLE TO ACHIEVE FOREIGN CAPITAL REQUIREMENTS FOR 1974 WITHOUT A REDUCTION IN THE CURRENT 10 YEAR MINIMUM TERMS. THE LARGER BANKS--CITY, CHASE, ITAU, REAL, ETC.--REPORT THAT FUNDS ARE AVAILABLE FOR BETTER CLIENTS AND THAT 10 YEAR MATURITY LIMITED OFFICIAL USE

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HAS NOT POSED SERIOUS PROBLEMS. SOME OF THE EUROPEAN BANKS AND LESS EXPERIENCED US BANK REPS SAY THAT 10 YEARS ARE "DIFFICULT". THEY HAVE ADOPTED MORE OF A WAIT AND SEE ATTITUDE, AND APPEAR WILLING TO GO 10 YEARS ONLY WITH BLUE CHIP CLIENTS AT ATTRACTIVE NET RATES. DESPITE THE UNDENIABLY TIGHTER SITUATION, SOME UNCERTAINTY AS TO SIZE OF BRAZIL'S TRADE DEFICIT THIS YEAR AND GREATER DEGREE OF CAUTION, WE HAVE NOT DETECTED ANY BASIC CHANGES IN THE MAJOR FOREIGN FINANCIAL INSTITUTIONS'

UNDERLYING CONFIDENCE IN BRAZIL. IT IS ADMITTEDLY A DIFFICULT JUDGMENT TO MAKE AT THIS POINT, BUT ON THE BASIS OF CONVERSATIONS AND IMPRESSIONS GLEANED FROM BANKERS AND BUSINESS CONTACTS OVER PAST TWO WEEKS, WE ARE INCLINED TO BELIEVE THAT BRAZIL WILL BE ABLE TO STICK WITH THE 10 YEAR REQUIREMENT FOR THE IMMEDIATE FUTURE.

7. WHILE THE KLONDIKE FEVER ATMOSPHERE OF 1973 HAS RECEDED, THE GENERAL ATMOSPHERE AS REFLECTED HERE IS ONE OF CONTINUED INTERNATIONAL CONFIDENCE.

8. COMMENT: EMBOFF HAS ALSO DISCUSSED IMPACT LIFTING 40 PERCENT DEPOSIT WITH PAULO LIRA, DIRECTOR, CENTER BANK. LIRA GAVE RELATIVELY OPTIMISTIC ASSESSMENT, STATING THAT BRAZIL EXPECTS TO ATTRACT SUFFICIENT FOREIGN FUNDS TO FINANCE INCREASED 1974 CURRENT ACCOUNT DEFICIT. LIRA CONFIRMED THAT CENTRAL BANK HAS RECEIVED SUBSTANTIAL LOAN REGISTRATION REQUESTS IMMEDIATELY FOLLOWING SUSPENSION OF DEPOSIT BUT THAT THIS REFLECTED MAINLY BACKLOG OF APPLICATIONS. WITH RESPECT TO 10 YEAR TERMS, LIRA NOTED THAT CENTRAL BANK IS FLEXIBLE ON THIS AND THAT IF SUFFICIENT FUNDS CANNOT BE ATTRACTED THE BANK WILL CONSIDER REDUCING TERMS BELOW 10 YEARS.
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